The Real Estate ANALYST

MAY 28
1957

Volume XXVI

Number 21

As I see it

IS THIS THE END OF AN ERA ?

THERE are many times when it is easy to guess what will happen. Whenever a well-pronounced trend has developed there is always a very great chance that the trend will continue in the same direction. This has been particularly true in real estate, where the trends are more regular and are longer than they are in many other types of economic data. The big chance of being wrong, however, in forecasting is when trends are changing, or when some of the trends are rising and others falling.

As pointed out in the April 30, 1957, Trends Bulletin, for the first time in 14 years, our national index of real estate activity has dropped below the normal line. In the past when this has occurred it has generally been the signal for a rather lengthy period of readjustment. I think it is important that we try to determine, as quickly as possible, whether the patterns of the past will be repeated or whether other factors in the economy have changed so greatly that this drop in real estate activity below the normal line can no longer have forecasting ability.

When the Trends Bulletin was published last month, real estate activity was only a fraction of a point below the normal line. The current figures, however, show that in the past month it has dropped, until now it is 6.0% below normal. The size of this drop in comparison with the figures of the past is shown on the chart at the bottom of pages 219 and 220.

In the table to the left below I am showing the number of nonfarm real estate transfers in thousands for January, February, March, and April of the last 3

NONFARM REAL ESTATE TRANSFERS
000 omitted

	1957	1956	1955
Jan.	394	428	444
Feb.	389	427	438
Mar.	388	416	431
Apr.	373	407	429
	1,544	1,678	1,742

	1928	1929	1930
Jan.	-	287	255
Feb.	-	275*	211**
Nov.	283	266	-
Dec.	284	256	-

*4-mo. total 1,129 **4-mo. total 988

years. In these months in 1957 there were 134,000 fewer transfers than there were in 1956, and 198,000 fewer than there were in 1955.

In the last real estate readjustment period, real estate activity dropped below the normal in November 1929. The table to the right on page 217 shows the number of nonfarm real estate transfers in the 4 months which followed, compared with the corresponding 4 months of the preceding year. Real estate transfers in the first 4 months below normal were 141,000 less than they were 1 year before.

There is no question that a large portion of the drop in transfers in 1957 is due to the smaller number of new houses coming on the market. The building figures would indicate that there are about 75,000 fewer dwelling units being completed in the 4 months ending with April than there were in the same 4 months of 2 years ago, and 64,000 fewer than in the corresponding period of a year ago. This would account for a great part of the drop in the number of voluntary transfers of nonfarm real estate.

Dwelling unit figures on a national basis, month by month, are not available for 1928 and 1929, but from such figures on individual cities which are available on a monthly basis it can easily be seen that the drop in the number of dwelling units during this period was proportionately greater in relationship to transfers than it has been in the period that has just ended. This would lead us to believe that the statement that real estate activity has gone below normal because of the reduced amount of building is no more valid than the same statement would have been in 1929 as an explanation of the drop and a reason why the subnormal activity would not continue.

It is, of course, still far too soon to say definitely that insofar as real estate goes the last few months mark the end of an era, but if the drop in activity continues for the next few months, it is entirely probable that the biggest real estate boom we have ever had has reached its end, and that we are now in the period of readjustment. This should not be too great a shock to persons in many parts of the United States, as the charts in the April 30, 1957, Real Estate Analyst showed that the boom had definitely ended in the Southwest and the West Coast some time ago. Some of the other areas have been practically on the normal line for some months.

Readjustments in the real estate field can be severe or relatively slight. In the last 100 years there have been only two really severe real estate readjustments, the first being the big depression of the 1870's and the second the big depression of the 1930's. These two readjustments were so great that they swept almost everything before them. Values dropped so radically that almost all mortgages got into trouble, and in each period foreclosures skyrocketed. The other readjustments in the real estate field during the past 100 years, while they have not varied greatly in length, have brought about only slight reductions in value, with relatively few foreclosures. These readjustment periods have been

characterized more by lack of activity i
readjustments in price.

On first glance it might appear that
the same characteristics which carried
1930's to extreme heights. Each of th
severe inflation which carried real estat
higher than those which preceded the bo
closures soared.

Since 1939 we have undergone a gre
either of these other two periods. It i
tion of the dollar during this inflationar
before. Rightly or wrongly, the Govern
in its control to prevent major drops in t
is that, should unemployment develop, in
enough to prevent major price readjus
drive the value of the dollar still lower,
be reduced to a point considerably belo

There are many positive factors in
our present belief that the readjustmen

A number of times last year and this
ation in regard to the trends in the sellin
in the cost of building new housing. In th
for these trends to be similar. An incre
followed by an increase in the selling pr
on variations in selling prices from 1913
1957, "As I See" Bulletin.) During 195
residential buildings were rising, and

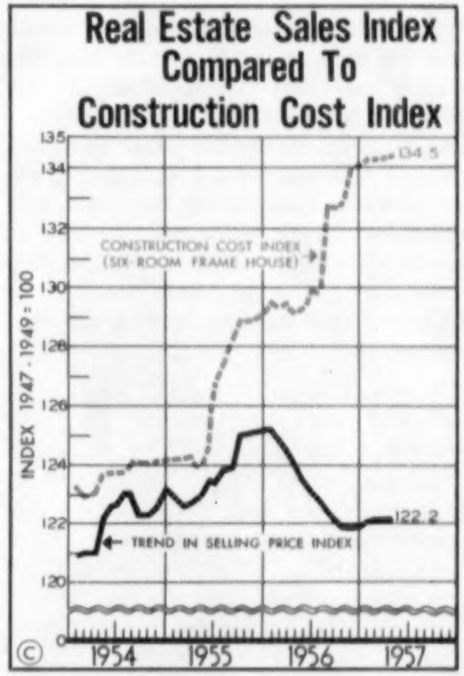
f activity in the real estate market than by drastic

ppear that any developing readjustment might have ch carried the readjustments of the 1870's and the Each of those readjustments followed a period of l real estate values and mortgages to levels greatly eded the boom. When these values dropped, fore-

rgone a greater amount of inflation than preceded riods. It is probable, however, that the devalua- inflationary period is more permanent than it was the Government is now committed to use all means r drops in the price and wage level. The probability develop, inflationary policies will be started quickly ce readjustments. Of course, this will eventually still lower, and during the next boom period it will rably below its present purchasing power.

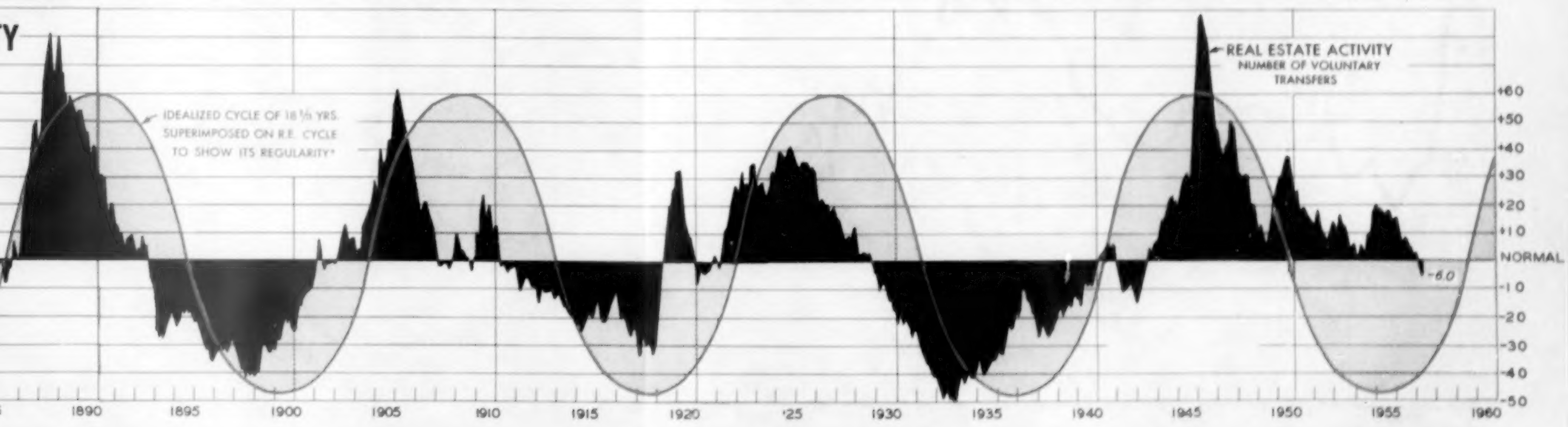
factors in today's picture which would strengthen adjustment will be relatively minor.

ar and this I have pointed out a rather peculiar situ- n the selling prices of existing housing and the trends sing. In the past there has been a marked tendency . An increase in construction cost has always been selling price of existing buildings. (See the chart from 1913 through 1956, on page 14 of the January 1, During 1956, however, construction costs on new ising, and the selling prices of existing buildings were dropping consistently. I said then that I believed that these divergent trends could not continue. Either construction costs must stop rising, or the values of existing buildings must stop falling. This assumption on my part has apparently been correct, as shown by the chart to the right. After falling all of last year and moving sideways this spring, the values of existing buildings are now rising slightly. If construction costs continue to rise, it seems logical that the selling prices of existing buildings will also continue to rise.



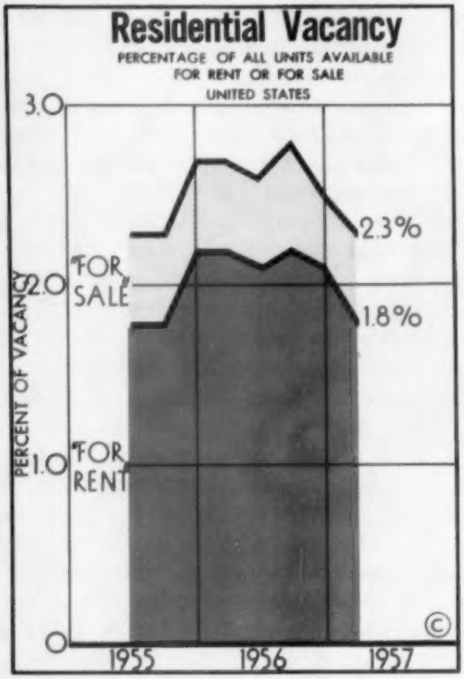
This probability is increased by the behavior of the index of new housing starts. On the chart of new private housing starts, shown at the bottom of page 221, I have superimposed some dashed lines indicating what I think might be considered the outside limits of the normal variation in the building rate, without showing a change in trend. The increase from a rate of 880,000 dwelling units in March to 940,000 in April comes within this normal band of fluctuations, and would not yet indicate that the decline has stopped. Should the May figure push the rate above our dashed line, I believe that it will be an indication (to be tested and weighed by succeeding months) that the trend has changed.

I am not at all convinced, however, that the drop in private housing starts so

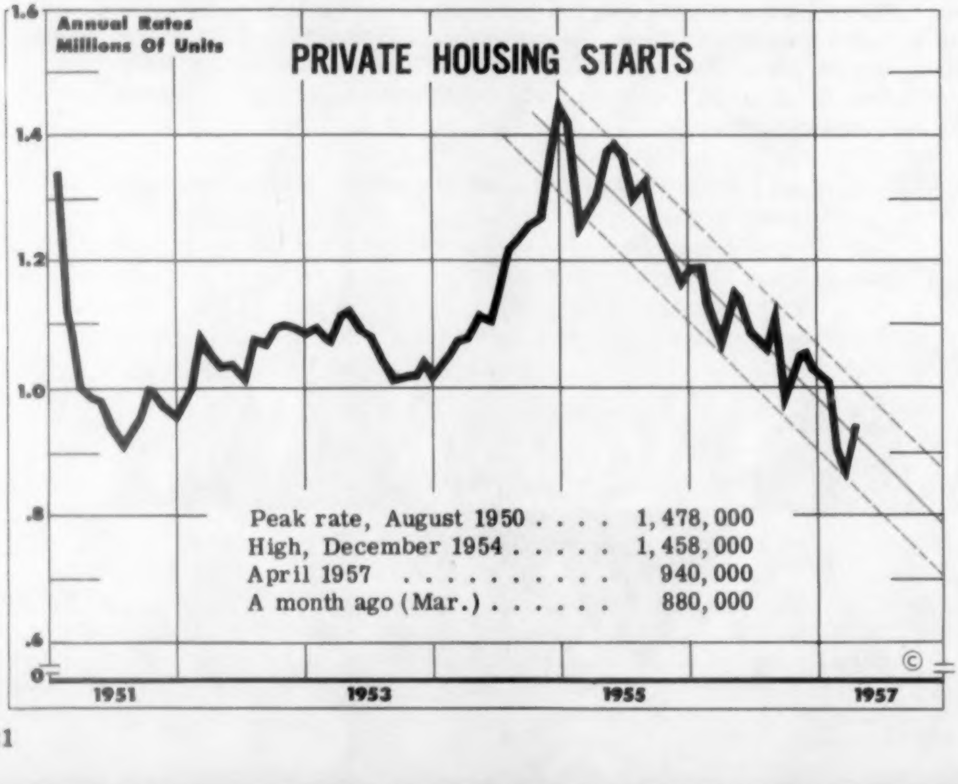


far has been the unmixed curse which many persons in the home building and building material field naturally believe it to be. I believe that the reduced volume during the past year particularly has had a very stabilizing effect on vacancies, which have actually decreased during this period, and is also partly responsible for the improved position of older houses referred to in the earlier part of this discussion.

National vacancy figures are available on a quarterly basis from the United States Census only from the second quarter of 1955. The chart to the right shows how vacancy has decreased, and the vacancy charted here is net vacancy, excluding unoccupied units which are not actually for rent or for sale. It also excludes all dilapidated and seasonal housing.



(cont. on following page)



Peak rate, August 1950	1,478,000
High, December 1954	1,458,000
April 1957	940,000
A month ago (Mar.)	880,000

The most certain way to depress the volume of home building over a period of years would be to continue building at a rapid rate in excess of the rate of absorption. We have paid bitterly during the past 10 years or more for artificial stimulation of agricultural production above the rate of consumption. A large part of our present agricultural budget is to keep agricultural prices high, which restricts the demand, both foreign and domestic, and increases foreign competition. If we seriously overbuild the market, increasing vacancy will have a tendency to create the situation on existing housing which we had last year, when sales prices were dropping, in spite of rising construction costs. If a situation of this sort continues for any length of time, the better buys in existing housing in comparison with the more expensive cost of new building create a dampening effect on the demand for new construction. Unless a building is worth as much as it cost to build in comparison with other buildings on the market, only special custom building will result, and the mass market is gone.

One other mitigating factor in any readjustment we may have to go through is that most of our mortgages are now on an amortized basis, precluding the necessity of refinancing in a period when refinancing might not be possible.

If the longest real estate boom in history is over, all policies should be reexamined, as the policies needed to succeed in a readjustment period are far different than those which succeeded during the boom.

Watch the figures carefully during the next few months, as we should know shortly whether the low figures of the past few months are really significant or a false alarm.

ROY WENZLICK